

(3) *Time of inclusion.* (i) For taxable years beginning before January 1, 1977, the amount of net income determined under subparagraph (2) is includible in the gross income of the individual for the taxable year in which it is received. The amount of net income thus distributed is subject to the tax imposed by section 408(f)(1) for the year includible in gross income.

(ii) [Reserved]

(4) *Example.* The provisions of this paragraph may be illustrated by the following example:

Example. On January 1, 1975, A, age 55, who is a calendar-year taxpayer, contributes \$1,500 to an individual retirement account established for his benefit. For 1975, A is entitled to a deduction of \$1,400 under section 219. For 1975, A does not claim as deductions any other items listed in section 62. A's gross income for 1975 is \$9,334. On April 1, 1976, \$107 is distributed to A from his individual retirement account. As of such date, the balance of the account is \$1,498 [\$1,605 - \$107]. There were no other distributions from the account as of such date. The net amount of income earned by the account is \$105 [\$1,498 + \$107 - (0 + \$1,500)]. The net income attributable to the excess contribution is \$7. [\$105 × (\$100/\$1,500)]. A's adjusted gross income for 1975 is his gross income for 1975 (\$9,334) reduced by the amount allowable to A as a deduction under section 219 (\$1,400), or \$7,934. A will include the \$7 of the \$107 distributed on April 1, 1976, in his gross income for 1976. Further, A will pay an additional income tax of \$.70 for 1976 under section 408(f)(1).

(d) *Deemed distribution*—(1) *General rule.* In any case in which an individual retirement account ceases to be an individual retirement account by reason of the application of section 408(e)(2), paragraph (a)(1) of this section shall apply as if there were a distribution on the first day of the taxable year in which such account ceases to be an individual retirement account of an amount equal to the fair market value on such day of all of the assets in the account on such day. In the case of a deemed distribution from an individual retirement annuity, see § 1.408-3(d).

(2) *Using account as security.* In any case in which an individual for whose benefit an individual retirement account is established uses, directly or indirectly, all or any portion of the account as security for a loan, paragraph (a)(1) of this section shall apply as if there were distributed on the first day

of the taxable year in which the loan was made an amount equal to that portion of the account used as security for such loan.

(e) *Distribution of annuity contracts.* Paragraph (a)(1) of this section does not apply to any annuity contract which is distributed from an individual retirement account and which satisfies the requirements of paragraphs (b) (1), (3), (4) and (5) of section 408. Amounts distributed under such contracts will be taxable to the distributee under section 72. For purposes of applying section 72 to a distribution from such a contract, the investment in such contract is zero.

(f) *Treatment of assets distributed from an individual retirement account for the purchase of an endowment contract.* Under section 408(e)(5), if all, or any portion, of the assets of an individual retirement account are used to purchase an endowment contract described in § 1.408-3(e) for the benefit of the individual for whose benefit the account is established—

(1) The excess, if any, of the total amount of assets used to purchase such contract over the portion of the assets attributable to life insurance protection shall be treated as a rollover contribution described in section 408(d)(3), and

(2) The portion of the assets attributable to life insurance protection shall be treated as a distribution described in paragraph (a)(91) of this section, except that the provisions of section 408(f) shall not apply to such amount.

(g) *Transfer incident to divorce*—(1) *General rule.* The transfer of an individual's interest, in whole or in part, in an individual retirement account, individual retirement annuity, or a retirement bond, to his former spouse under a valid divorce decree or a written instrument incident to such divorce shall not be considered to be a distribution from such an account or annuity to such individual or his former spouse; nor shall it be considered a taxable transfer by such individual to his former spouse notwithstanding any other provision of Subtitle A of the Code.

(2) *Spousal account.* The interest described in this paragraph (g) which is

transferred to the former spouse shall be treated as an individual retirement account of such spouse if the interest is an individual retirement account; an individual retirement annuity of such spouse if such interest is an individual retirement annuity; and a retirement bond of such spouse if such interest is a retirement bond.

[T.D. 7714, 45 FR 52793, Aug. 8, 1980]

§ 1.408-5 Annual reports by trustees or issuers.

(a) *In general.* The trustee of an individual retirement account or the issuer of an individual retirement annuity shall make annual calendar year reports concerning the status of the account or annuity. The report shall contain the information required in paragraph (b) and be furnished or filed in the manner and time specified in paragraph (c).

(b) *Information required to be included in the annual reports.* The annual calendar year report shall contain the following information for transactions occurring during the calendar year—

- (1) The amount of contributions;
- (2) The amount of distributions;
- (3) In the case of an endowment contract, the amount of the premium paid allocable to the cost of life insurance;
- (4) The name and address of the trustee or issuer; and
- (5) Such other information as the Commissioner may require.

(c) *Manner and time for filing.* (1) The annual report shall be furnished to the individual on whose behalf the account is established or in whose name the annuity is purchased (or the beneficiary of the individual or owner). The report shall be furnished on or before the 30th day of June following the calendar year for which the report is required.

(2) The Commissioner may require the annual report to be filed with the Service at the time the Commissioner specifies.

(d) *Penalties.* Section 6693 prescribes penalties for failure to file the annual report.

(e) *Effective date.* This section shall apply to reports for calendar years after 1978.

(f) *Reports for years prior to 1979.* For years prior to 1979, a trustee or issuer

shall make reports in the time and manner as the Commissioner requires.

[T.D. 7714, 45 FR 52795, Aug. 8, 1980]

§ 1.408-6 Disclosure statements for individual retirement arrangements.

(a) *In general.*—(1) *General rule.* Trustees and issuers of individual retirement accounts and annuities are, under the authority of section 408(i), required to provide disclosure statements. This section sets forth these requirements.

(2) [Reserved]

(b)–(c) [Reserved]

(d) *Requirements.* (1)—(3) [Reserved]

(4) *Disclosure statements.*—(i) Under the authority contained in section 408(i), a disclosure statement shall be furnished in accordance with the provisions of this subparagraph by the trustee of an individual retirement account described in section 408(a) or the issuer of an individual retirement annuity described in section 408(b) or of an endowment contract described in section 408(b) to the individual (hereinafter referred to as the “benefited individual”) for whom such an account, annuity, or contract is, or is to be, established.

(ii)(A)(1) The trustee or issuer shall furnish, or cause to be furnished, to the benefited individual, a disclosure statement satisfying the requirements of subdivisions (iii) through (viii) of this subparagraph, as applicable, and a copy of the governing instrument to be used in establishing the account, annuity, or endowment contract. The copy of such governing instrument need not be filled in with financial and other data pertaining to the benefited individual; however, such copy must be complete in all other respects. The disclosure statement and copy of the governing instrument must be received by the benefited individual at least seven days preceding the earlier of the date of establishment or purchase of the account, annuity, or endowment contract. A disclosure statement or copy of the governing instrument required by this subparagraph may be received by the benefited individual less than seven days preceding, but no later than, the earlier of the date of establishment or purchase, if the benefited individual is permitted to revoke the account, annuity, or endowment contract pursuant to a procedure which

satisfies the requirements of subdivision (ii)(A)(2) of this subparagraph.

(2) A procedure for revocation satisfies the requirements of this subdivision (ii)(A)(2) of this subparagraph if the benefited individual is permitted to revoke the account, or endowment contract by mailing or delivering, at his option, a notice of revocation on or before a day not less than seven days after the earlier of the date of establishment or purchase and, upon revocation, is entitled to a return of the entire amount of the consideration paid by him for the account, annuity, or endowment contract without adjustment for such items as sales commissions, administrative expenses or fluctuation in market value. The procedure may require that the notice be in writing or that it be oral, or it may require both a written and an oral notice. If an oral notice is required or permitted, the procedure must permit it to be delivered by telephone call during normal business hours. If a written notice is required or permitted, the procedure must provide that, if mailed, it shall be deemed mailed on the date of the postmark (or if sent by certified or registered mail, the date of certification or registration) if it is deposited in the mail in the United States in an envelope, or other appropriate wrapper, first class postage prepaid, properly addressed.

(B) If after a disclosure statement has been furnished, or caused to be furnished, to the benefited individual pursuant to paragraph (d)(4)(ii)(A) of this section and—

(1) On or before the earlier of the date of establishment or purchase, or

(2) On or before the last day on which the benefited individual is permitted to revoke the account, annuity, or endowment contract (if the benefited individual has a right to revoke the account, annuity, or endowment contract pursuant to the rules of subdivision (ii)(A) of this subparagraph).

there becomes effective a material adverse change in the information set forth in such disclosure statement or a material change in the governing instrument to be used in establishing the account, annuity, or contract, the trustee or issuer shall furnish, or cause to be furnished, to the benefited indi-

vidual such amendments to any previously furnished disclosure statement or governing instrument as may be necessary to adequately inform the benefited individual of such change. The trustee or issuer shall be treated as satisfying this subdivision (ii)(B) of this subparagraph only if material required to be furnished by this subdivision is received by the benefited individual at least seven days preceding the earlier of the date of establishment or purchase of the account, annuity, or endowment contract or if the benefited individual is permitted to revoke the account, annuity, or endowment contract on or before a date not less than seven days after the date on which such material is received, pursuant to a procedure for revocation otherwise satisfying the provisions of subdivision (ii)(A)(2) of this subparagraph.

(C) If the governing instrument is amended after the account, annuity, or endowment contract is no longer subject to revocation pursuant to subdivision (ii)(A) or (B) of this subparagraph, the trustee or issuer shall not later than the 30th day after the later of the date on which the amendment is adopted or becomes effective, deliver or mail to the last known address of the benefited individual a copy of such amendment and, if such amendment affects a matter described in subdivisions (iii) through (viii) of this subparagraph, a disclosure statement with respect to such matter meeting the requirements of subdivision (iv) of this subparagraph.

(D) For purposes of subdivision (ii)(A) and (B) of this subparagraph, if a disclosure statement, governing instrument, or an amendment to either, is mailed to the benefited individual, it shall be deemed (in the absence of evidence to the contrary) to be received by the benefited individual seven days after the date of mailing.

(E) In the case of a trust described in section 408(c) (relating to certain retirement savings arrangements for employees or members of associations of employees), the following special rules shall be applied:

(1) For purposes of this subparagraph, references to the benefited individual's account, annuity, or endowment contract shall refer to the benefited individual's interest in such trust, and

(2) The provisions of subdivision (ii) of this subparagraph shall be applied by substituting "the date on which the benefited individual's interest in such trust commences" for "the earlier of the date of establishment or purchase" wherever it appear therein.

Thus, for example, if an employer establishes a trust described in section 408(c) for the benefit of employees, and the trustee furnishes an employee with a disclosure statement and a copy of the governing instrument (as required by this subparagraph) on the date such employee's interest in the trust commences, such employee must be given a right to revoke such interest within a period of at least seven days. If any contribution has been made within such period (whether by the employee or by the employer), the full amount of such contribution must be paid to such employee pursuant to subdivision (ii)(A)(2) of this subparagraph.

(iii) The disclosure statement required by this subparagraph shall set forth in nontechnical language the following matters as such matters relate to the account, annuity, or endowment contract (as the case may be);

(A) Concise explanations of—

(1) The statutory requirements prescribed in section 408(a) (relating to an individual retirement account) or section 408(b) (relating to an individual retirement annuity and an endowment contract), and any additional requirements (whether or not required by law) that pertain to the particular retirement savings arrangement.

(2) The income tax consequences of establishing an account, annuity, or endowment contract (as the case may be) which meets the requirements of section 408(a) relating to an individual retirement account) or section 408(b) (relating to an individual retirement annuity and an endowment contract), including the deductibility of contributions to, the tax treatment of distributions (other than premature distributions) from, the availability of income tax free rollovers to and from, and the tax status of such account, annuity, or endowment contract.

(3) The limitations and restrictions on the deduction for retirement savings under section 219, including the ineligibility of certain individuals who

are active participants in a plan described in section 219(b)(2)(A) or for whom amounts are contributed under a contract described in section 219(b)(2)(B) to make deductible contributions to an account or for an annuity or endowment contract.

(4) The circumstances under which the benefited individual may revoke the account, annuity, or endowment contract, and the procedure therefor (including the name, address, and telephone number of the person designated to receive notice of such revocation). Such explanation shall be prominently displayed at the beginning of the disclosure statement.

(B) Statements to the effect that—

(1) If the benefited individual or his beneficiary engages in a prohibited transaction, described in section 4975(c) with respect to an individual retirement account, the account will lose its exemption from tax by reason of section 408(e)(2)(A), and the benefited individual must include in gross income, for the taxable year during which the benefited individual or his beneficiary engages in the prohibited transaction the fair market value of the account.

(2) If the owner of an individual retirement annuity or endowment contract described in section 408(b) borrows any money under, or by use of, such annuity or endowment contract, then, under section 408(e)(3), such annuity or endowment contract loses its section 408(b) classification, and the owner must include in gross income, for the taxable year during which the owner borrows any money under, or by use of, such annuity or endowment contract, the fair market value of the annuity or endowment contract.

(3) If a benefited individual uses all or any portion of an individual retirement account as security for a loan, then, under section 408(e)(4), the portion so used is treated as distributed to such individual and the benefited individual must include such distribution in gross income for the taxable year during which he so uses such account.

(4) An additional tax of 10 percent is imposed by section 408(f) on distributions (including amounts deemed distributed as the result of a prohibited loan or use as security for a loan) made

before the benefited individual has attained age 59½, unless such distribution is made on account of death or disability, or unless a rollover contribution is made with such distribution.

(5) Sections 2039(e) (relating to exemption from estate tax of annuities under certain trusts and plans) and 2517 (relating to exemption from gift tax of specified transfers of certain annuities under qualified plans) apply (including the manner in which such sections apply) to the account, annuity, or endowment contract.

(6) Section 402(a)(2) and (e) (relating to tax on lump sum distributions) is not applicable to distributions from an account, annuity, or endowment contract.

(7) A minimum distribution is required under section 408(a) (6) or (7) and 408(b) (3) or (4) (including a brief explanation of the amount of minimum distribution) and that if the amount distributed from an account, annuity, or endowment contract during the taxable year of the payee is less than the minimum required during such year, an excise tax, which shall be paid by the payee, is imposed under section 4974, in an amount equal to 50 percent of the excess of the minimum required to be distributed over the amount actually distributed during the year.

(8) An excise tax is imposed under section 4973 on excess contributions (including a brief explanation of an excess contribution).

(9) The benefited individual must file Form 5329 (Return for Individual Retirement Savings Arrangement) with the Internal Revenue Service for each taxable year during which the account, annuity, or endowment contract is maintained.

(10) The account or contract has or has not (as the case may be) been approved as to form for use as an account, annuity, or endowment contract by the Internal Revenue Service. For purposes of this subdivision, if a favorable opinion or determination letter with respect to the form of a prototype trust, custodial account, annuity, or endowment contract has been issued by the Internal Revenue Service, or the instrument which establishes an individual retirement trust account or an individual retirement custodial ac-

count utilizes the precise language of a form currently provided by the Internal Revenue Service (including any additional language permitted by such form), such account or contract may be treated as approved as to form.

(11) The Internal Revenue Service approval is a determination only as to the form of the account, annuity, or endowment contract, and does not represent a determination of the merits of such account, annuity, or endowment contract.

(12) The proceeds from the account, annuity or endowment contract may be used by the benefited individual as a rollover contribution to another account or annuity or retirement bond in accordance with the provisions of section 408(d)(3).

(13) In the case of an endowment contract described in section 408(b), no deduction is allowed under section 219 for that portion of the amounts paid under the contract for the taxable year properly allocable to the cost of life insurance.

(14) If applicable, in the event that the benefited individual revokes the account, annuity, or endowment contract, pursuant to the procedure described in the disclosure statement (see subdivision (A)(4) of this subdivision (iii)), the benefited individual is entitled to a return of the entire amount of the consideration paid by him for the account, annuity, or endowment contract without adjustment for such items as sales commissions, administrative expenses or fluctuation in market value.

(15) Further information can be obtained from any district office of the Internal Revenue Service.

To the extent that information on the matters described in subdivisions (iii) (A) and (B) of this subparagraph is provided in a publication of the Internal Revenue Service relating to individual retirement savings arrangements, such publication may be furnished by the trustee or issuer in lieu of providing information relating to such matters in a disclosure statement.

(C) The financial disclosure required by paragraph (d)(4) (v), (vi), and (vii) of this section.

(iv) In the case of an amendment to the terms of an account, annuity, or

endowment contract described in paragraph (d)(4)(i) of this section, the disclosure statement required by this subparagraph need not repeat material contained in the statement furnished pursuant to paragraph (d)(4)(iii) of this section, but it must set forth in non-technical language those matters described in paragraph (d)(4)(iii) of this section which are affected by such amendment.

(v) With respect to an account, annuity, or endowment contract described in paragraph (d)(4)(i) of this section (other than an account or annuity which is to receive only a rollover contribution described in paragraph (d)(4)(vi) of this section and to which no deductible contributions will be made), the disclosure statement must set forth in cases where either an amount is guaranteed over period of time (such as in the case of a non-participating endowment or annuity contract), or a projection of growth of the value of the account, annuity, or endowment contract can reasonably be made (such as in the case of a participating endowment or annuity contract (other than a variable annuity) or pass-book savings account), the following:

(A) To the extent that an amount is guaranteed,

(1) The amount, determined without regard to any portion of a contribution which is not deductible, that would be guaranteed to be available to the benefited individual if (i) level annual contributions in the amount of \$1,000 were to be made on the first day of each year, and (ii) the benefited individual were to withdraw in a single sum the entire amount of such account, annuity, or endowment contract at the end of each of the first five years during which contributions are to be made, at the end of the year in which the benefited individual attains the ages of 60, 65, and 70, and at the end of any other year during which the increase of the guaranteed available amount is less than the increase of the guaranteed available amount during any preceding year for any reason other than decrease or cessation of contributions, and

(2) A statement that the amount described in subdivision (v)(A)(1) of this

subparagraph is guaranteed, and the period for which guaranteed;

(B) To the extent a projection of growth of the value of the account, annuity, or endowment contract can reasonably be made but the amounts are not guaranteed.

(1) The amount, determined without regard to any portion of a contribution which is not deductible, and upon the basis of an earnings rate no greater than, and terms no different from, those currently in effect, that would be available to the benefited individual if (i) level annual contributions in the amount of \$1,000 were to be made on the first day of each year, and (ii) the benefited individual were to withdraw in a single sum the entire amount of such account, annuity, or endowment contract at the end of each of the first five years during which contributions are to be made, at the end of each of the years in which the benefited individual attains the ages of 60, 65, and 70, and at the end of any other year during which the increase of the available amount is less than the increase of the available amount during any preceding year for any reason other than decrease or cessation of contributions, and

(2) A statement that the amount described in paragraph (d)(4)(v)(B)(1) of this section is a projection and is not guaranteed and a statement of the earnings rate and terms on the basis of which the projection is made;

(C) The portion of each \$1,000 contribution attributable to the cost of life insurance, which would not be deductible, for each year during which contributions are to be made; and

(D) The sales commission (including any commission attributable to the sale of life insurance), if any, to be charged in each year, expressed as a percentage of gross annual contributions (including any portion attributable to the cost of life insurance) to be made for each year.

(vi) With respect to an account or annuity described in paragraph (d)(4)(i) of this section to which a rollover contribution described in section 402(a)(5)(A), 403(a)(4)(A), 408(d)(3)(A) or 409(b)(3)(C) will be made, the disclosure statement must set forth, in cases where an amount is guaranteed over a

period of time (such as in the case of a non-participating annuity contract, or a projection of growth of the value of the account or annuity can reasonably be made (such as in the case of a participating annuity contract (other than a variable annuity) or a passbook savings account), the following:

(A) To the extent guaranteed,

(1) The amount that would be guaranteed to be available to the benefited individual if (i) Such a rollover contribution in the amount of \$1,000 were to be made on the first day of the year, (ii) No other contribution were to be made, and (iii) The benefited individual were to withdraw in a single sum the entire amount of such account or annuity at the end of each of the first five years after the contribution is made, at the end of the year in which the benefited individual attains the ages of 60, 65, and 70, and at the end of any other year during which the increase of the guaranteed available amount is less than the increase of the guaranteed available amount during any preceding year, and

(2) A statement that the amount described in paragraph (d)(vi)(A)(1) of this section is guaranteed;

(B) To the extent that a projection of growth of the value of the account or annuity can reasonably be made but the amounts are not guaranteed,

(1) The amount, determined upon the basis of an earnings rate no greater than, and terms no different from, those currently in effect, that would be available to the benefited individual if (i) such a rollover contribution in the amount of \$1,000 were to be made on the first day of the year, (ii) no other contribution were to be made, and (iii) the benefited individual were to withdraw in a single sum the entire amount of such account or annuity at the end of each of the first five years after the contribution is made, at the end of each of the years in which the benefited individual attains the ages 60, 65, 70, and at the end of any other year during which the increase of the available amount is less than the increase of the available amount during any preceding year, and

(2) A statement that the amount described in paragraph (d)(4)(vi)(B) (1) of this section is a projection and is not

guaranteed and a statement of the earnings rate and terms on the basis of which the projection is made; and

(C) The sales commission, if any, to be charged in each year, expressed as a percentage of the assumed \$1,000 contribution.

(vii) With respect to an account, annuity, or endowment contract described in paragraph (d)(4)(i) of this section, in all cases not subject to paragraph (d)(4) (v) or (vi) of this section (such as in the case of a mutual fund or variable annuity), the disclosure statement must set forth information described in subdivisions (A) through (C) of this subdivisions (vii) based (as applicable with respect to the type or types of contributions to be received by the account, annuity, or endowment contract) upon the assumption of (1) level annual contributions of \$1,000 on the first day of each year, (2) a rollover contribution of \$1,000 on the first day of the year and no other contributions, or (3) a rollover contribution of \$1,000 on the first day of the year plus level annual contributions of \$1,000 on the first day of each year.

(A) A description (in nontechnical language) with respect to the benefited individual's interest in the account, annuity, or endowment contract, of:

(1) Each type of charge, and the amount thereof, which may be made against a contribution,

(2) The method for computing and allocating annual earnings, and

(3) Each charge (other than those described in complying with paragraph (d)(4)(vii)(A)(1) of this section) which may be applied to such interest in determining the net amount of money available to the benefited individual and the method of computing each such charge;

(B) A statement that growth in value of the account, annuity, or endowment contract is neither guaranteed nor projected; and

(C) The portion of each \$1,000 contribution attributable to the cost of life insurance, which would not be deductible, for every year during which contributions are to be made.

(viii) A disclosure statement, or an amendment thereto, furnished pursuant to the provisions of this subparagraph may contain information in addition to that required by paragraph (d)(4)(iii) through (vii) of this section. However, such disclosure statement will not be considered to comply with the provisions of this subparagraph if the substance of such additional material or the form in which it is presented causes such disclosure statement to be false or misleading with respect to the information required to be disclosed by this paragraph.

(ix) The provisions of section 6693, relating to failure to provide reports on individual retirement accounts or annuities, shall apply to any trustee or issuer who fails to furnish, or cause to be furnished, a disclosure statement, a copy of the governing instrument, or an amendment to either, as required by this paragraph.

(x) This section shall be effective for disclosure statements and copies of governing instruments mailed, or delivered without mailing, after February 14, 1977.

(xi) This section does not reflect the amendments made by section 1501 of the Tax Reform Act of 1976 (90 Stat. 1734) relating to retirement savings for certain married individuals.

[T.D. 7714, 45 FR 52795, Aug. 8, 1980; 45 FR 56802, Aug. 26, 1980]

§ 1.408-7 Reports on distributions from individual retirement plans.

(a) *Requirement of report.* The trustee of an individual retirement account or the issuer of an individual retirement annuity who makes a distribution during any calendar year to an individual from such account or under such annuity shall make a report on Form W-2P (in the case of distributions that are not total distributions) or Form 1099R (in the case of total distributions), and their related transmittal forms, for such year. The return must show the name and address of the person to whom the distribution was made, the aggregate amount of such distribution, and such other information as is required by the forms.

(b) *Amount subject to this section.* The amounts subject to reporting under paragraph (a) include all amounts dis-

tributed or made available to which section 408(d) applies.

(c) *Time and place for filing.* The report required under this section for any calendar year shall be filed after the close of that year and on or before February 28 of the following year with the appropriate Internal Revenue Service Center.

(d) *Statement to recipients.* (1) Each trustee or issuer required to file Form 1099R or Form W-2P under this section shall furnish to the person whose identifying number is (or should be) shown on the forms a copy of the form.

(2) Each statement required by this paragraph to be furnished to recipients shall be furnished to such person after November 30 of the year of the distribution and on or before January 31 of the following year.

(e) *Effective date.* This section is effective for calendar years beginning after December 31, 1977.

[T.D. 7714, 45 FR 52798, Aug. 8, 1980]

§ 1.409-1 Retirement bonds.

(a) *In general.* Section 409 authorizes the issuance of bonds under the Second Liberty Bond Act the purchase price of which would be deductible under section 219. Section 409 also prescribes the tax treatment of such bonds. See paragraph (b) of this section.

(b) *Income tax treatment of bonds—*(1) *General rule.* Except as provided in paragraph (b)(2) of this section, the entire proceeds upon redemption of a retirement bond described in section 409(a) shall be included in the gross income of the taxpayer entitled to such proceeds. If a bond has not been tendered for redemption by the registered owner before the close of the taxable year in which he attains age 70½, he must include in his gross income for such taxable year the amount of the proceeds he would have received if the bond had been redeemed at age 70½. The provisions of sections 72 and 1232 do not apply to a retirement bond.

(2) *Exceptions.* (i) If a retirement bond is redeemed within 12 months after the issue date, the proceeds are excluded from gross income if no deduction is allowed under section 219 on account of the purchase of such bond. For definition of issue date, see 31 CFR 346.1(c).

(ii) If a retirement bond is redeemed after the close of the taxable year in which the registered owner attains age 70½ the proceeds from the redemption of the bond are excludable from the gross income of the registered owner or his beneficiary to the extent that such proceeds were includible in the gross income of the registered owner for such taxable year.

(iii) If a retirement bond is surrendered for reissuance in the same or lesser face amount, the difference between current redemption value of the bond surrendered for reissuance and the current surrender value of the bond reissued is includible in the gross income of the registered owner.

(3) *Basis.* The basis of a retirement bond is zero.

(c) *Rollover.* The first sentence of paragraph (b)(1) of this section shall not apply in any case in which a retirement bond is redeemed by the registered owner before the close of the taxable year in which he attains the age of 70½ if he transfers the entire amount of the proceeds of such redemption to—

(1) An individual retirement account described in section 408(a) or an individual retirement annuity described in section 408(b) (other than an endowment contract described in § 1.408-3(e)), or

(2) An employees' trust which is described in section 401(a) which is exempt from tax under section 501(a), or an annuity plan described in section 403(a), for the benefit of the registered owner, on or before the 60th day after the day on which he received the proceeds of such redemption. This subparagraph shall not apply in the case of a transfer to a trust or plan described in (c)(2) of this section unless no part of the purchase price of the retirement bond redeemed is attributable to any source other than a rollover contribution from such an employees' trust or annuity plan (other than an annuity plan or employees' trust forming part of a plan under which the individual was an employee within the meaning of section 401(c)(1) at the time contributions were made on his behalf under the plan).

(d) *Additional tax—(1) Early redemption.* Except as provided in paragraph

(d)(2) of this section, under section 409(c) if a retirement bond is redeemed by the registered owner before he attains age 59½, his tax under chapter 1 of the Code is increased by an amount equal to 10 percent of the proceeds of the redemption includible in his gross income for the taxable year. Except in the case of the credits allowable under sections 31, 39, or 42, no credit can be used to offset the tax described in the preceding sentence.

(2) *Limitations.* Paragraph (d)(1) of this section shall not apply if—

(i) During the taxable year of the registered owner in which a retirement bond is redeemed, the registered owner becomes disabled within the meaning of section 72(m)(7), or

(ii) A retirement bond is tendered for redemption in accordance with paragraph (b)(2)(i) of this section.

[T.D. 7714, 45 FR 52799, Aug. 8, 1980]

§ 1.410(a)-1 Minimum participation standards; general rules.

(a) *In general.* A plan is not a qualified plan (and a trust forming a part of such plan is not a qualified trust) unless the plan satisfies—

(1) The minimum age and service requirements of section 410(a)(1) and § 1.410(a)-3,

(2) The maximum age requirements of section 410(a)(2) and § 1.410(a)-4, and

(3) The minimum coverage requirements of section 410(b)(1) and § 1.410(b)-1.

(b) *Organization of regulations relating to minimum participation standards—(1) General rules.* This section prescribes general rules relating to the minimum participation standards provided by Section 410.

(2) *Effective dates.* Section 1.410(a)-2 provides rules under section 1017 of the Employee Retirement Income Security Act of 1974 relating to effective dates under section 410.

(3) *Age and service conditions.* Section 1.410(a)-3 provides rules under section 410(a)(1) relating to minimum age and service conditions.

(4) *Maximum age and time of participation.* Section 1.410(a)-4 provides rules under section 410(a)(2) and (4) relating to maximum age and time of participation.

(5) *Year of service; breaks in service.* For rules relating to years of service and breaks in service, see 29 CFR Part 2530 (Department of Labor regulations relating to minimum standards for employee pension benefit plans). See § 1.410(a)-5 for rules under section 410(a)(3)(B) relating to seasonal industries and for certain rules under section 410(a)(5) relating to breaks in service.

(6) *Breaks in service.* Section 1.410(a)-6 provides special rules under section 1017(f) of the Employee Retirement Income Security Act of 1974 relating to amendment of break in service rules.

(7) *Elapsed time.* Section 1.410 (a)-7 provides rules under sections 410 and 411 relating to the elapsed time method of crediting years of service.

(8) *Coverage.* Section 1.410(b)-1 provides rules relating to the minimum coverage requirements provided by section 410(b)(1).

(9) *Church election.* Section 1.410(d)-1 provides rules relating to the election by a church to have participation, vesting, funding, etc., provisions apply.

(c) *Application of participation standards to certain plans—(1) General rule.* Except as provided in subparagraph (2) of this paragraph, section 410 does not apply to—

(i) A governmental plan (within the meaning of section 414(d) and the regulations thereunder),

(ii) A church plan (within the meaning of section 414(e) and the regulations thereunder) which has not made the election provided by section 410(d) and the regulations thereunder,

(iii) A plan which has not provided for employer contributions at any time after September 2, 1974, and

(iv) A plan established and maintained by a society, order, or association described in section 501(c) (8) or (9), if no part of the contributions to or under such plan are made by employers of participants in such plan.

(2) *Participation requirements.* A plan described in subparagraph (1) of this paragraph shall, for purposes of section 401(a), be treated as meeting the requirements of section 410 if such plan meets the coverage requirements resulting from the application of section 401(a)(3) as in effect on September 1, 1974. Such coverage requirements in-

clude the rules in § 1.410(b)-1(d) (special rules relating to minimum coverage requirements), that interpret statutory provisions substantially identical to section 401(a)(3) as in effect on September 1, 1974. In applying the rules of that paragraph (d) to plans described in this paragraph (c) employees whose principal duties consist in supervising the work of other employees shall be treated as officers, shareholders, and highly compensated employees.

(d) *Supersession.* Section 1.410(a)-1 through 1.410(d)-1 inclusive, of the Temporary Income Tax Regulation under the Employee Retirement Income Security Act of 1974 are superseded by this section and §§ 1.410(a)-2 through 1.410(d)-1.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47193, Sept. 20, 1977, as amended by T.D. 7703, 45 FR 40980, June 17, 1980; T.D. 7735, 45 FR 74722, Nov. 12, 1980]

§ 1.410(a)-2 Effective dates.

(a) *Plans not in existence on January 1, 1974.* Under section 1017(a) of the Employee Retirement Income Security Act of 1974, in the case of a plan which was not in existence on January 1, 1974, section 410 and the regulations thereunder apply for plan years beginning after September 2, 1974. See paragraph (c) of this section for time plan is considered in existence.

(b) *Plans in existence on January 1, 1974.* Under section 1017(b) of the Employee Retirement Income Security Act of 1974, in the case of a plan which was in existence on January 1, 1974, section 410 and the regulations thereunder apply for plan years beginning after December 31, 1975. See paragraph (c) of this section for time plan is considered to be in existence.

(c) *Time of plan existence—(1) General rule.* For purposes of this section, a plan is considered to be in existence on a particular day if—

(i) The plan on or before that day was reduced to writing and adopted by the employer (including, in the case of a corporate employer, formal approval by the employer's board of directors and, if required, shareholder), even though no amounts had been contributed under the plan as of such day, and

(ii) The plan was not terminated on or before that day.

(2) *Collectively bargained plan.* Notwithstanding subparagraph (1) of this paragraph, a plan described in section 413(a), relating to a plan maintained pursuant to a collective bargaining agreement, is considered to be in existence on a particular day if—

(i) On or before that day there is a legally enforceable agreement to establish such a plan signed by the employer, and

(ii) The employer contributions to be made to the plan are set forth in the agreement.

(3) *Special rule.* If a plan is considered to be in existence on January 1, 1974, under subparagraph (1) of this paragraph, any other plan with which such existing plan is merged or consolidated shall also be considered to be in existence on such date.

(d) *Certain existing plans may elect new provisions—*(1) *In general.* The plan administrator (as defined in section 414(g)) of a plan that was in existence on January 1, 1974, may elect to have the provisions of the Code relating to participation, vesting, funding, and form of benefit (as in effect from time to time) apply to a plan year selected by the plan year selected by the plan administrator which begins after September 2, 1974, but before the otherwise applicable effective dates determined under section 1017 (b) or (c), 1021, or 1024 of the Employee Retirement Income Security Act of 1974, and to all subsequent plan years. The provisions referred to are the amendments to the Code made by sections 1011, 1012, 1013, 1015, 1016(a) (1) through (11) and (13) through (27), 1021, and 1022(b) of the Employee Retirement Income Security Act of 1974.

(2) *Election is irrevocable.* Any election made under this paragraph, once made shall be irrevocable.

(3) *Procedure and time for making election.* An election under this paragraph shall be made by attaching a statement to either the annual return required under section 6058(a) (or an amended return) with respect to the plan which is filed for the first plan year for which the election is effective or to a written request for a determination letter relating to the qualification of the plan under section 401(a), 403(a), or 405(a) of the Code and, if trustee, the exempt

status under section 501(a) of the Code of a trust constituting a part of the plan. If the election is made with a written request for a determination letter, the election may be conditioned upon issuance of a favorable determination letter and will become irrevocable upon issuance of such letter. The statement shall indicate that the election is made under section 1017(d) of the Employee Retirement Income Security Act of 1974 and the first plan year for which the election is effective.

(e) *Examples.* The rules of this section are illustrated by the following examples:

Example (1). A plan is adopted on January 2, 1974, effective as of January 1, 1974. The plan is not considered to have been in existence on January 1, 1974.

Example (2). A plan was in existence on January 1, 1974, and was amended on November 1, 1974, to increase benefits. The fact that the plan was amended is not relevant and the amended plan is considered to be in existence on January 1, 1974.

Example (3). (i) A subsidiary business corporation is a member of a controlled group of corporations within the meaning of IRC section 1563(a). On November 1, 1974, the plan of the parent corporation is amended to provide coverage for employees of the subsidiary corporation. This amendment of the parent corporation's plan does not affect the effective date of section 410 with respect to the parent corporation's plan. No distinction is made for this purpose between employees of the parent corporation and employees of the subsidiary corporation.

(ii) If the subsidiary adopted a separate plan on November 1, 1974, under paragraph (a) of this section, section 410 would apply to that plan for its first plan year beginning after September 2, 1974. However, the adoption of a different plan by the subsidiary would not affect the time section 410 applies to the plan of the parent corporation. If, instead of adopting its own separate plan, the subsidiary merely executed an adoption agreement under the terms of the parent plan providing that a subsidiary, upon the execution of an adoption agreement, will become part of the parent plan, the effective date of section 410 with respect to such plan will not be affected by the adoption of the plan by the subsidiary.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47194, Sept. 20, 1977]

§ 1.410(a)-3 Minimum age and service conditions.

(a) *General rule.* Except as provided by paragraph (b) or (c) of this section,

a plan is not a qualified plan (and a trust forming a part of such plan is not a qualified trust) if the plan requires, as a condition of participation in the plan, that an employee complete a period of service with the employer or employers maintaining the plan extending beyond the later of—

(1) *Age 25.* The date on which the employee attains the age of 25; or

(2) *One year of service.* The date on which the employee completes 1 year of service.

(b) *Special rule for plan with 3-year 100 percent vesting.* A plan which provides that after not more than 3 years of service each participant's right to his accrued benefit under the plan is completely nonforfeitable (within the meaning of section 411 and the regulations thereunder) at the time such benefit accrues satisfies the requirements of paragraph (a) of this section if the period of service required by the plan as a condition of participation does not extend beyond the later of—

(1) *Age 25.* The date on which the employee attains the age of 25; or

(2) *Three years of service.* The date on which the employee completes 3 years of service.

(c) *Special rule for employees of certain educational institutions.* A plan maintained exclusively for employees of an educational institution (as defined in section 170(b)(1)(A)(ii)) by an employer exempt from tax under section 501(a) which provides that after 1 year of service each participant's right to his accrued benefit under the plan is completely nonforfeitable (within the meaning of section 411 and the regulations thereunder) at the time such benefit accrues satisfies the requirements of paragraph (a) of this section if the period of service required by the plan as a condition of participation does not extend beyond the later of—

(1) *Age 30.* The date on which the employee attains the age of 30; or

(2) *One year of service.* The date on which the employee completes 1 year of service.

(d) *Other conditions.* Section 410(a), § 1.410(a)-4, and this section relate solely to age and service conditions and do not preclude a plan from establishing conditions, other than conditions relating to age or service, which must be

satisfied by plan participants. For example, such provisions would not preclude a qualified plan from requiring, as a condition of participation, that an employee be employed within a specified job classification. See section 410(b) and the regulations thereunder for rules with respect to coverage of employees under qualified plans.

(e) *Age and service requirements—(1) General rule.* For purposes of applying the rules of this section, plan provisions may be treated as imposing age or service requirements even though the provisions do not specifically refer to age or service. Plan provisions which have the effect of requiring an age or service requirement with the employer or employers maintaining the plan will be treated as if they imposed an age or service requirement. In general, a plan under which an employee cannot participate unless he retires will impose an age and service requirement. However, a plan may provide benefits which supplement benefits provided for employees covered under a pension plan, as defined in section 3(2) of the Employee Retirement Income Security Act of 1974, satisfying the requirements of section 410(a)(1) without violating the age and service rules.

(2) *Examples.* The rules of this paragraph are illustrated by the following examples:

Example (1). Corporation A is divided into two divisions. In order to work in division 2 an employee must first have been employed in division 1 for 5 years. A plan provision which required division 2 employment for participation will be treated as a service requirement because such a provision has the effect of requiring 5 years of service.

Example (2). Plan B requires as a condition of participation that each employee have had a driver's license for 15 years or more. This provision will be treated as an age requirement because such a provision has the effect of requiring an employee to attain a specified age.

Example (3). A plan which requires 1 year of service as a condition of participation also excludes a part-time or seasonal employee if his customary employment is for not more than 20 hours per week or 5 months in any plan year. The plan does not qualify because the provision could result in the exclusion by reason of a minimum service requirement of an employee who has completed a year of service. The plan would not qualify even though after excluding all such employees,

the plan satisfied the coverage requirements of section 410(b).

Example (4). Employer A establishes a plan which covers employees after they retire and does not cover current employees unless they retire. Any employee who works past age 60 is treated as retired. The plan fails to satisfy the requirements of section 410(a) because the plan imposes a minimum age and service requirement in excess of that allowed by this section.

Example (5). Employer B establishes plan X, which provides that employees covered by qualified plan Y will receive benefits supplementing their benefits under plan Y to take into account cost of living increases after retirement. Plan X is not treated as imposing an age of service requirement.

Example (6). Employer C establishes a qualified plan satisfying the minimum age and service requirements. At a later time, entry into the plan is frozen so that employees not covered at that time cannot participate in the plan. The limitation on new participants is not treated as imposing a minimum age and service requirement.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47194, Sept. 20, 1977]

§ 1.410(a)-3T Minimum age and service conditions (temporary).

(a) [Reserved]

(b) *Special rule for plan with 2-year 100 percent vesting.* A plan which provides that after not more than 2 years of service each participant's right to his or her accrued benefit under the plan is completely nonforeitable (within the meaning of section 411 and the regulations thereunder) at the time such benefit accrues satisfies the requirements of paragraph (a) of this section if the period of service required by the plan as a condition of participation does not extend beyond the later of—

(1) [Reserved]

(2) *Two years of service.* The date on which the employee completes 2 years of service. For employees not described in § 1.411(a)-3T(e)(1), which describes employees with one hour of service in any plan year beginning after December 31, 1988, or later in the case of certain collectively bargained plans, the preceding sentence shall be applied by substituting "3 years of service" for "2 years of service".

[T.D. 8170, 53 FR 239, Jan. 6, 1988]

§ 1.410(a)-4 Maximum age conditions and time of participation.

(a) *Maximum age conditions—(1) General rule.* A plan is not a qualified plan (and a trust forming a part of such plan is not a qualified trust) if the plan excludes from participation (on the basis of age) an employee who has attained an age specified by the plan unless—

(i) The plan is a defined benefit plan or a target benefit plan, and

(ii) The employee begins employment with the employer after the employee has attained an age specified by the plan, which age is not more than 5 years before normal retirement age (within the meaning of section 411(a)(8) and § 1.411(a)-7.

For purposes of this paragraph, a target benefit plan is a defined contribution plan under which the amount of employer contributions allocated to each participant is determined under a plan formula which does not allow employer discretion and on the basis of the amount necessary to provide a target benefit specified by the plan for such participant. Such target benefit must be the type of benefit which is provided by a defined benefit plan and the targeted benefit must not discriminate in favor of employees who are officers, shareholders, or highly compensated. For purposes of this paragraph, in the determination of the time an employee begins employment, any such time which is included in a period of service which may be disregarded under the break in service rules need not be taken into account.

(2) *Examples.* The rules provided by this paragraph are illustrated by the following examples:

Example (1). A defined benefit plan provides that an employee will become a participant upon completion of 3 years of service if at such time the employee is less than age 60. The normal retirement age under the plan is age 65. The plan also provides full and immediate vesting for each of the plan's participants. Under the plan, an employee hired at age 58 would be denied participation on account of service for the first 3 years and on account of maximum age for the remaining years even though the employee was hired more than 5 years prior to the normal retirement date. The plan therefore does not satisfy section 410(a)(2).

Example (2). A defined benefit plan provides a normal retirement age of the later of

age 65 or completion of 10 years of service. Because no employee could ever be hired within 5 years of his normal retirement age, the plan could not exclude employees for being over a specified age.

Example (3). Prior to the effective date of section 410, a defined benefit plan with a normal retirement age of 65 contained a maximum age 55 requirement for participation. Because of the maximum age requirement, and employee hired at age 58 was excluded from the plan. This employee is age 61 at the time that section 410 first applies to the plan. The employee cannot be excluded from participation because of age. The exclusion under section 410(a)(2) is not applicable in this instance because the employee's age at the time of hire, 58, was not within 5 years of the normal retirement age specified in the plan.

Example (4). Employee A was hired at age 50 and participated in a defined benefit plan until separating from service at age 55 with 5 years of service and with no vested benefit. At age 61, employee A was rehired within 5 years of the normal retirement age of 65 after he incurred 6 consecutive breaks in service. Because A's consecutive number of 1-year breaks (6) exceeds his years of service prior to such breaks (5), his service before the breaks may be disregarded. Consequently, A's initial employment date falling within such period may be disregarded and the plan could exclude A on account of his age because his employment commenced within 5 years of normal retirement age.

(b) *Time of participation*—(1) *General rule.* A plan is not a qualified plan (and a trust forming a part of such plan is not a qualified trust) unless under the plan any employee who has satisfied the applicable minimum age and service requirements specified in § 1.410(a)-3, and who is otherwise entitled to participate in the plan, commences participation in the plan no later than the earlier of—

(i) The first day of the first plan year beginning after the date on which such employee first satisfied such requirements, or

(ii) The date 6 months after the date on which he first satisfied such requirements,

unless such employee was separated from service and has not returned before the date referred to in subdivision (i) or (ii), whichever is applicable. If such separated employee returns to service after either of such dates without incurring a 1-year break in service, the employee must commence partici-

pation immediately upon his return. In the case of a plan using the elapsed time method described in § 1.410(a)-7, such an employee who has a period of absence commencing before the date referred to in subdivision (i) or (ii) (whichever is applicable) must commence participation as of such applicable date no later than the date such absence ended. However, if an employee's prior service is disregarded on account of the plan's break-in-service rules then, for purposes of this subparagraph, such service is also disregarded for purposes of determining the date on which such employee first satisfied the minimum age and service requirements.

(2) *Examples.* The rules provided by this paragraph are illustrated by the following examples:

Example (1). A calendar year plan provides that an employee may enter the plan only on the first semi-annual entry date, January 1 or July 1, after he has satisfied the applicable minimum age and service requirements specified in section 410(a)(1). The plan satisfies the requirements of this paragraph because an employee is eligible to participate no later than the earlier of (1) the first day of the first plan year beginning after he satisfied the applicable minimum age and service requirements, or (2) the date 6 months after he satisfied such requirements.

Example (2). A plan provides that an employee is not eligible to participate until the first day of the first plan year beginning after he has satisfied the minimum age and service requirements of section 410(a)(1). In this case, an employee who satisfies the "6 month" rule described in subparagraph (1) of this paragraph will not be eligible to participate in the plan. Therefore, the plan does not satisfy the requirements of this paragraph.

Example (3). A calendar year plan provides that an employee may enter the plan only on the first semi-annual entry date, January 1 or July 1, after he has satisfied the applicable minimum age and service requirements specified in section 410(a)(1). Employee A after 10 years of service separated from service in 1976 with a vested benefit. On February 1, 1990, A returns to employment covered by the plan. Assuming A completes a year of service after his return, A must participate immediately on his return, February 1. A's prior service cannot be disregarded, because he had a vested benefit when he separated from service. Therefore, the plan may not postpone his participation until July 1.

Example (4). Assume the same facts as in example (3). The plan has the break-in-service rule described in section 410(a)(5)(D) and

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§ 1.410(a)-5(c)(4). Employee B, after he had 5 years of service but no vested benefit incurs 5 consecutive 1-year breaks. Because B's prior service can be disregarded, the plan may postpone B's participation in the plan under the rule described in section 410(a)(4) and this paragraph.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47195, Sept. 20, 1977, as amended by T.D. 7703, 45 FR 40980, June 17, 1980]

§ 1.410(a)-5 Year of service; break in service.

(a) *Year of service.* For the rules relating to years of service under subparagraphs (A), (C), and (D) of section 410(a)(3), see regulations prescribed by the Secretary of Labor under 29 CFR Part 2530, relating to minimum standards for employee pension benefit plans.

Rules relating to a general rule for a year of service, hours of service, and maritime industries apply for purposes of section 410(a) and the regulations thereunder.

(b) *Seasonal industries.* For rules which relate to seasonal industries under section 410(a)(3)(B), see regulations prescribed by the Secretary of Labor under 29 CFR Part 2530, relating to minimum standards for employee pension benefits plans.

(c) *Breaks in service—(1) General rule.* This paragraph provides rules with respect to breaks in service under section 410(a)(5). Except as provided in subparagraphs (2), (3), (4), and (5) of this paragraph, all of an employee's years of service with the employer or employers maintaining a plan are taken into account in computing his period of service under the plan for purposes of section 410(a)(1) and § 1.410(a)-3.

(2) *Employees under 3-year 100 percent vesting schedule—(i) General rule.* In the case of an employee who incurs a 1-year break in service under a plan which provides that after not more than 3 years of service, each participant's right to his accrued benefit under the plan in completely non-forfeitable (within the meaning of section 411 and the regulations thereunder) at the time such benefit accrues, the employee's service before the break in service is not required to be taken into account after the break in service in determining the employ-

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ee's years of service under section 410(a)(1) and § 1.410(a)-3 if such employee has not satisfied such service requirement.

(ii) *Example.* The rules of this subparagraph are illustrated by the following example.

Example. A qualified plan computing service by the actual counting of hours provides full and immediate vesting. The plan can not require as a condition of participation that an employee complete 3 consecutive years of service with the employer because the requirement as to consecutive years is not permitted under section 410(a) (5). However, such a plan can require 3 years without a break in service, i.e., 3 years with no intervening years in which the employee fails to complete more than 500 hours of service. Under a plan containing such a participation requirement, the following example illustrates when employees would become eligible to participate.

Year	Hours of service completed		
	Employee A	Employee B	Employee C
1	1,000	1,000	1,000
2	1,000	1,000	500
3	1,000	700	1,000
4	1,000	1,000	700
5	1,000	1,000	1,000
6	1,000	1,000	1,000

NOTE.—Employee A will have satisfied the plan's service requirement at the end of year 3. Employee B at the end of year 4, and Employee C at the end of year 6.

(3) *One-year break in service—(i) In general.* In computing the period of service of an employee who has incurred a 1-year break in service, for purposes of section 410(a)(1) and § 1.410(a)-3, a plan may disregard the employee's service before the break until the employee completes a year of service after such break in service.

(ii) *Examples.* The rules provided by this subparagraph are illustrated by the following examples.

Example (1). Employee A completes a year of service under a plan computing service by the actual counting of hours for the 12-month period ending December 31, 1980, and incurs a 1-year break in service for the 12-month period ending December 31, 1981. The plan does not contain the provisions permitted by section 410(a)(5)(B) (relating to 3-year 100 percent vesting) and section 410(a)(5)(D) (relating to nonvested participants). Thereafter, he does not complete a year of service. As of January 1, 1982, in computing his period of service under the plan his service prior to December 31, 1981, is not

required to be taken into account for purposes of section 410(a)(1) and § 1.410(a)-3.

Example (2). The employee in example (1) completes a year of service for the 12-month period ending December 31, 1982. Prior to December 31, 1982, in computing the employee's period of service as of any date occurring in 1982, the employee's service before December 31, 1981, is not required to be taken into account for purposes of section 410(a)(1) and § 1.410(a)-3. Because the employee completed a year of service for the 12-month period ending December 31, 1982, however, his period of service is redetermined as of January 1, 1982. Upon completion of a year of service for 1982, the employee's period of service, determined as of any date occurring in 1982, includes service prior to December 31, 1981.

(4) *Nonvested participants*—(i) *General rule.* In the case of a participant in a plan who does not have any nonforfeitable right under the plan to his employer-derived accrued benefit and who incurs a 1-year break in service, for purposes of section 410(a)(1) and § 1.410(a)-3 the plan may disregard his years of service prior to such break if the number of his consecutive 1-year breaks in service equals or exceeds his aggregate number of years of service prior to such break. In the case of a plan using the elapsed time method described in Department of Labor regulations, the plan may disregard such years of service prior to such break if the period of severance is at least 1 year and the period of severance equals or exceeds the prior period of service, whether or not consecutive, completed before such period of severance. The plan may in computing such aggregate number of years of service prior to such break disregard any years of service which could have been disregarded under this subparagraph by reason of any prior break in service.

(ii) *Examples.* The rules of this subparagraph are illustrated by the following example:

Example. In 1980, A, who was hired at age 35, separates from the service of X Corporation after completing 4 years of service. At this time A had no vested benefits. In 1985, after incurring 5 consecutive one-year breaks in service, A was reemployed. Under section 410(a)(5)(D), A's 4 years of service may be disregarded because they are exceeded by the number of years of consecutive one-year breaks (5) after such service.

(d) *Special continuity rule for certain plans.* For special rules for computing

years of service in the case of a plan maintained by more than one employer, see regulations prescribed by the Secretary of Labor under 29 CFR Part 2530, relating to minimum standards for employee pension benefit plans.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47196, Sept. 20, 1977; T.D. 7508, 42 FR 57123, Nov. 1, 1977, as amended by T.D. 7703, 45 FR 40980, June 17, 1980]

§ 1.410(a)-6 Amendment of break in service rules; Transition period.

(a) *In general.* Under section 1017(f) (1) of the Employee retirement Income Security Act of 1974, a plan is not a qualified plan (and a trust forming a part of such plan is not a qualified trust) if the rules of the plan relating to breaks in service are amended, and—

(1) Such amendment is effective after January 1, 1974, and before the date on which section 410 becomes applicable to the plan, and

(2) Under such amendment, any employee's participation in the plan commences at any date later than the later of—

(i) The date on which his participation would commence under the break in service rules of section 410(a)(5), or

(ii) The earliest date on which his participation would commence under the plan as in effect on or after January 1, 1974.

(b) *Break in service rules.* For purposes of paragraph (a), the term "break in service rules" means the rules provided by a plan relating to circumstances under which a period of an employee's service or plan participation is disregarded for purposes of determining his rights to participate in the plan, if under such rules such service is disregarded by reason of the employee's failure to complete a required period of service within a specified period of time.

(Sec. 410 (88 Stat. 898; 26 U.S.C. 410))

[T.D. 7508, 42 FR 47197, Sept. 20, 1977; 43 FR 2721, Jan. 19, 1978]

§ 1.410(a)-7 Elapsed time.

(a) *In general*—(1) *Introduction to elapsed time method of crediting service.*

(i) 29 CFR 2530.200b-2 sets forth the general method of crediting service for an